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SUBJECT: SCENESETTER: CANADA AND THE SPP

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(D) Ottawa 1029 (E) Ottawa 999

1. (U) This is the first in a series of cables offering Mission views and background information on elements of the Security and Prosperity Partnership. This cable outlines some political and economic factors in Canada that may affect progress toward SPP goals.

2. (SBU) Summary: The Security and Prosperity Partnership has met with applause from major groups within Canada, although some interest groups are critical. On the security side, we are building on the solid foundation of the Smart Border process, and Canadian policy will continue to be driven by the desire to meet U.S. security needs to keep the border open and moving.

On the prosperity side, the government's course is less well-charted. A growing anxiety about Canada's continued access to U.S. markets has fueled a lively debate over the last few years on how to build on NAFTA, and business groups have welcomed SPP as the first step on that road. Regulatory cooperation enjoys broad support from business but will continue to raise sovereignty concerns among traditional opponents of freer trade.

Despite GOC commitment to SPP, there are management and political obstacles on the Canadian side to early major results. They include potential resistance from the agencies responsible for making the regulatory changes; weaknesses in the Canadian regulatory process, and growing threats to survival of the Martin government. Finally, the SPP prosperity agenda does not address the elephants outside the tent: Canadian frustration with NAFTA dispute settlement and the continuing ban on live cattle imports. SPP will therefore not necessarily be seen as a major win for Canada, and the Martin government has not attempted to sell it as a "big bang" breakthrough. However, a set of pragmatic and balanced deliverables could create momentum for continuing and perhaps tackling bigger challenges through the SPP process.

The Security Agenda: Broad Support, Hard Problems

3. (SBU) A broad consensus, and developed bilateral framework, supports the objectives outlined in the security agenda. The Smart Border Action Plan, initiated in 2001, created a successful framework for systematically addressing border issues. The Smart Border concept enjoys broad support among business and local governments on both sides of the border as well as in Ottawa, and has been an important element in rebuilding public confidence that security and trade can go hand in hand. The current government has aggressively reorganized Canadian security and border agencies and has backed up its commitment to border security with CAD 1 billion in new funding for border security in the 2005 budget.

5. (SBU) For the GOC, the hardest part of the border equation will be addressing infrastructure bottlenecks, which result as much from trade growth as from new security requirements, while balancing the interests of a multitude of provincial, municipal and private stakeholders. The difficulty of finding popular and affordable solutions to infrastructure problems makes it likely that the GOC will continue to look for procedural fixes, such as reverse clearance and other proposals to move processing away from the border, some of which may be problematic for us. Canadian entry procedures for goods also continue to concentrate processing on the border, making entry more cumbersome than under the U.S. system.

6. (SBU) While ministers have repeatedly expressed their determination to prevent terrorist attacks on the U.S. from within Canada, and have allocated considerable resources to

maritime and aviation security, so far they seem to be less concerned about potential dangers coming north by land. DPM McLellan is resisting calls from Canadian customs and law enforcement unions to beef up or streamline its balkanized border apparatus, divided between unarmed customs officers and thinly spread RCMP detachments responsible for enforcement (Ref C).

Prosperity Agenda: A Path Less Clear

17. (SBU) For the past few years, Canadian officials, academics and private sector representatives have been conducting a lively debate on the future of Canada's trade policy. After ten years of NAFTA, which have shifted Canada's economy onto an even more pronounced North-South axis, few people here doubt that relations with the U.S. are central to Canada's future as a trading nation. The GOC's efforts to expand markets elsewhere, which include negotiating initiatives with various Asian and Latin countries as well as a nebulous framework agreement with the EU, cannot substantially alter that reality. At the same time, early, rapid trade gains under NAFTA have moderated; Canadian exports to the U.S. began to stagnate in the new millennium and have only recently returned to 2000 levels, and the rising Canadian dollar has generated anxiety about future export trends. Having absorbed the early benefits of NAFTA, many Canadians have begun to focus on its shortcomings, notably its failure to restrain U.S. antidumping and countervailing duty actions (despite the fact that this was never an element of the agreement). Concern about the "border effect", which predated but was vastly heightened by 9/11, has shaken Canadian confidence in the security of its access to its prime export market, and the BSE crisis and softwood lumber dispute have strengthened doubts about the ability of NAFTA institutions to protect Canadian interests.

18. (SBU) Arguments about the best course to pursue with the U.S. have fallen into two major categories: the "big bang" and the "incrementalist" approach. In the first category, groups such as the Canadian Council of Chief Executives have offered a range of ambitious options, including a "North American security perimeter" in which border and defense policies would be harmonized in order to allow trade to flow freely, and a customs union. The incrementalists, who include the Canadian Chamber of Commerce, have argued that no political will exists on either side for grand projects, and that pragmatically addressing individual barriers one by one would be more feasible and cost-effective. In that context, the "prosperity" side of the SPP may be seen as an endorsement of the incrementalist approach.

19. (SBU) Regardless of their previous positions, major business groups have applauded SPP and are eager to support implementation, particularly since they do not want this initiative to lose momentum. On the regulatory side, the private sector is solidly in favor of harmonizing North American standards to the extent possible. The private-sector Executive Advisory Committee on Smart Regulation (Ref B.) told GOC policymakers frankly that the norm should be development of North American standards, even if that meant, in many cases, adopting U.S. standards.

110. (SBU) This view, however, is not universal. Despite occasional admissions that some U.S. regulatory mechanisms, for example in the environmental arena, may well outperform Canada's, many Canadians tend to assume that Canada is generally cleaner, healthier and safer than the U.S. (Even U.S. policies and programs, such as Energy Star, that are adopted by Canada are often assumed to be of Canadian origin. In the same vein, Canadian opposition to oil exploration in ANWR allows many Canadians to feel morally superior, while ignoring the impact of energy development in the Canadian wilderness.) The "Smart Regulation" initiative has already aroused the ire of traditional anti-trade groups and those concerned about Canadian sovereignty. Sounding a familiar note, Maude Barlow of the (economic nationalist) Council of Canadians predicted that SPP would have dire effects on Canadian sovereignty and the privacy of individual Canadians. Among other things, she charged that SPP would "strip Canada of its ability to set safe standards for its citizens". Mixed press response to SPP also reflected, along with support for closer engagement, traditional concerns about sovereignty and distrust of the U.S.

111. (SBU) Aside from lingering pockets of opposition to economic integration per se, the GOC may also face a struggle in moving change quickly through its regulatory apparatus. While Canadian regulatory processes follow a process similar to that of the U.S., with PCO retaining the oversight and coordination role of OMB, central coordination appears to be considerably weaker. Private sector critics, among them Smart Regulation advisors, charge that current regulatory processes are too stovepiped and do not generate adequate outside input, even from other GOC agencies. The

Smart Regulation program envisions various institutional changes to address this problem, including a stronger mandate for PCO, but it remains a work in (early) progress.

12. (SBU) The domestic political atmosphere may also make it difficult for the GOC to achieve quick progress on regulatory issues. Martin's minority government has faced repeated challenges in recent months, with a no-confidence measure seemingly always around the corner. In the current round, explosive revelations from an ongoing public inquiry, pointing to a pattern of government kickbacks to the Liberal Party, have already distracted the government and could well result in a vote of no confidence by the end of the year. The opposition has already flexed its muscles in other areas. In a major rebuff, Parliament vetoed a government order separating International Trade Canada from Foreign Affairs, leaving Canada's trade negotiators in legal limbo after almost a year of frantic administrative revamping and personnel shifts. Growing conflict with provinces over fiscal issues (ref D) will also affect progress on any broader regulatory reform program. Provinces, which play a major role in regulation, may resist Ottawa's attempts to press them into international commitments.

Conclusion

13. (SBU) Despite these complicating factors, SPP clearly offers a framework to move forward pragmatically on trade barriers and irritants and to promote our existing border agenda. There is potential synergy between SPP goals and Canada's Smart Regulation initiative. Moreover, SPP can help fold in and raise the profile of productive bilateral discussions already underway in areas such as energy, agriculture and the environment, providing a welcome balance to endless coverage of trade disputes. We believe it will remain a priority for the GOC; PCO officials have already made it clear that they will continue to coordinate and press Canadian departments for results. (Details on PCO's plans for organizing the Canadian end of SPP will follow septel.)

14. (SBU) In the long term, an established process, and the pressure to produce results in advance of high-level meetings, can help us attack regulatory issues more systematically. However, in the meantime the inherent value of stronger regulatory cooperation is likely to continue to be overshadowed by the elephants outside the tent: the long-running dispute over U.S. antidumping and countervailing duties on softwood and the continued closure of the border to live cattle imports, which are sapping enthusiasm for free trade in some of its strongest former constituencies. The risk remains that voters affected by major trade problems will resent a bilateral initiative that appears to require Canadian concessions but does not deliver on their big concerns, a point we need to take into account as we develop the SPP agenda.